85-1803

NO.

Supreme Court, U.S.
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CLERK

IN THE

Supreme Court of the United States

OCTOBER TERM, 1985

SLAB FORK COAL COMPANY,
Petitioner,

v.

UNITED VIRGINIA BANK,
KANAWHA VALLEY BANK, N.A., and
THE CHARLESTON NATIONAL BANK,
Respondent.

PETITION FOR A WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE FOURTH CIRCUIT

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5cpy

QUESTIONS PRESENTED

1. Whether the United States Court of Appeals for the Fourth Circuit erred in ruling that revenues generated by Petitioner's post-petition performance under a contract are subject to the Respondents' pre-petition security interest in the contract?

2. Whether the United States Court of Appeals for the Fourth Circuit erred in extending the Respondents' pre-petition security interest in contract rights to include monies generated by the Petitioner's post-petition performance of a contract, thereby frustrating the rehabilitative nature and purpose of the Bankruptcy Reform Act of 1978?

3. Whether the United States Court of Appeals for the Fourth Circuit erred in applying the expanded definition of cash collateral under § 363(a) of the Bankruptcy Amendment and Federal Judgeship Act of 1984, 11 U.S.C. § 363(a), in ruling that monies generated by Petitioner's post-petition performance under a contract which is the subject of a pre-petition security interest are cash collateral?

PARTIES BELOW

The Petitioner in this case who participated in the case below is:

Slab Fok Coal Company

The other parties in the case below were:

United Virginia Bank
Kanawha Valley Bank, N.A.
The Charleston National Bank

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IN THE
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No.

SLAB FORK COAL COMPANY,
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v.

UNITED VIRGINIA BANK,
KANAWHA VALLEY BANK, N.A., and
THE CHARLESTON NATIONAL BANK,
Respondent.

PETITION FOR A WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE FOURTH CIRCUIT

Slab Fork Coal Company ("Slab Fork") petitions for a Writ of Certiorari to review a decision of the United States Court of Appeals for the Fourth Circuit. The decision of the United States Court of Appeals for the Fourth Circuit erroneously interpreted the provisions of § 363(a) and § 552 of the Bankruptcy Code, 11 U.S.C. §§ 363(a) and 552.

OPINIONS AND ORDERS BELOW

The decision of the United States Court of Appeals for the Fourth Circuit in United Virginia Bank; Kanawha Valley Bank, N.A.; The Charleston National Bank v. Slab Fork Coal Company is reported at 784 F.2d 1188. That decision is set forth in Appendix A. The Order of the United States District Court for the Southern District of West Virginia is unreported and is set forth in Appendix B. The Order of the United States Bankruptcy Court for the Southern District of West Virginia is unreported and is set forth in Appendix C.

JURISDICTION

The decision of the Court of Appeals for the Fourth Circuit was entered on March 3, 1986. Slab Fork invokes the jurisdiction of this Court under 28 U.S.C. § 1254(1).

STATUTES INVOLVED

The decision of the Court of Appeals for the Fourth Circuit reversed the decision of the United States District Court for the Southern District of West Virginia which interpreted §§ 363(a) and 552 of the Bankruptcy Code, 11 U.S.C. §§ 363(a) and 552.

STATEMENT OF THE CASE

Slab Fork is a West Virginia corporation which was engaged in the mining of coal in Raleigh and Wyoming Counties, West Virginia, since 1907.

On March 14, 1983, United Virginia Bank, Kanawha Valley Bank, N.A., and The Charleston National Bank (hereinafter collectively referred to as "the Banks") filed an involuntary petition under Chapter 7 of the Bankruptcy Code against Slab Fork. At the time of such filing, Slab

Fork was indebted to the Banks for an amount in excess of $12,000,000 arising from a Letter of Credit and Note Exchange Agreement executed by the parties on June 1, 1981, (hereinafter referred to as the "Loan Agreement"). Pursuant to the terms of the Loan Agreement, Slab Fork granted the Banks a security interest in various collateral including all accounts arising from the sale of coal and proceeds thereof, all accounts, general intangibles, chattel paper, documents, instruments, inventory and the proceeds thereof. Slab Fork did not grant a security interest in its coal reserves or coal leases. The Banks properly perfected their security interest in the collateral by filing financing statements in the appropriate locations as determined by the Uniform Commercial Code as enacted in West Virginia.

On April 8, 1983, an Order for Relief under Chapter 11 of the Bankruptcy Code was entered by the United States Bankruptcy Court for the Southern District of West Virginia. Slab Fork has at all times remained in possession of its property, and on August 8, 1983, filed its proposed disclosure statement and plan of reorganization. One of Slab Fork's primary assets and the asset upon which its plan of reorganization is structured is a coal supply agreement dated March 1, 1956, between Slab Fork and Armco Steel Corporation, now Armco, Inc., (said agreement hereinafter referred to as the "Armco contract").

In late February, 1983, extreme financial difficulties forced Slab Fork to shut down its mining operations. As a result, in early March, 1983, Slab Fork suspended its coal shipments to Armco; the suspension was treated as an event of

excusable default under the Armco contract. At that point in time, Slab Fork had no available monies to mine coal or to ship coal to Armco. In order to preserve the Armco contract, on April 1, 1983, Slab Fork executed a contract mining agreement with Maben Energy Corporation (hereinafter "Maben") whereby Maben agreed to mine and deliver coal for the account of Slab Fork to Armco. Shipments were resumed to Armco beginning with the week of April 18, 1983.

As of March 14, 1983, Armco owed Slab Fork $993,730.98 for coal mined and delivered prior to the filing of the petition. These monies which were subject to the Banks' pre-petition security interest were paid to the Banks.

On May 24, 1983, the Banks filed a Motion to Prohibit Use of Cash Collateral in the United States Bankruptcy Court for the Southern District of West Virginia.

Specifically, the Banks sought to prohibit Slab Fork's use of the accounts receivable and monies generated post-petition under the Armco contract. A hearing was held on such motion on June 30, 1983. At the hearing, the Banks clarified their position and stated that they sought to direct Slab Fork to pay over the excess cash collateral to the Banks, that is, the monies remaining after the costs of mining the coal had been deducted from the revenues received from Armco.

By Order dated July 11, 1983, the United States Bankruptcy Court for the Southern District of West Virginia denied the Banks' motion finding that neither the revenue from the Armco contract nor the expectation of future funds from Armco was "cash collateral" within the purview of § 363 of the Bankruptcy Code.

By Order dated February 2, 1985, the United States District Court for the Southern District of West Virginia affirmed the Bankruptcy Court's decision denying the Banks' motion to prohibit Slab Fork's use of cash collateral. The District Court expressly determined that the post-petition monies generated under the Armco contract were controlled by the general rule of § 552(a) of the Bankruptcy Code, 11 U.S.C. § 552(a), and did not meet any of the exceptions set forth in 11 U.S.C. § 552(b). The Court also found that the post-petition revenues generated by Slab Fork were not cash collateral within the meaning of § 363(a) of the Bankruptcy Code, 11 U.S.C. § 363(a), and therefore were not subject to the Banks' security interest in the Armco contract.

On March 3, 1986, the United States Court of Appeals for the Fourth Circuit

reversed the decision of the District Court. The Fourth Circuit held that the revenues generated under the Armco contract after the filing of the petition were proceeds of the Armco contract and were thus subject to the Banks' pre-petition security interest in the Armco contract. The Fourth Circuit further held that under the definition of cash collateral found in the Bankruptcy Amendment and Federal Judgeship Act of 1984, the post-petition revenues generated under the Armco contract constituted cash collateral. The Fourth Circuit remanded the case to the Bankruptcy Court to evaluate the equities of the case under § 552(b) of the Bankruptcy Code, 11 U.S.C. § 552(b), and to determine the appropriate balance between the rights of the secured and unsecured creditors.

REASONS FOR GRANTING THE WRIT

A. The Post-Petition Effect of a Security Interest Issue.

This Court has not decided the effect of a security interest granted in pre-petition collateral on property received by a debtor-in-possession post-petition. The District Court for the Southern District of West Virginia ruled that the monies generated post-petition under the Armco contract constituted after-acquired property and, therefore, under 11 U.S.C. § 552(a) were not subject to the Banks' pre-petition lien. The Fourth Circuit ruled that the monies generated post-petition under the Armco contract were proceeds of the Armco contract and thus were subject to the Banks' lien under 11 U.S.C. § 552(b). The decisions interpreting the scope and extent of 11 U.S.C. § 552(b) are in conflict. This case affords the Court the opportunity to

interpret the applicability of 11 U.S.C. § 552(b) on property received by a debtor post-petition and thus resolve this important issue.

Section 552 of the Bankruptcy Reform Act of 1978, 11 U.S.C. § 552, which sets forth the post-petition effect of a security interest provides:

> (a) Except as provided in subsection (b) of this section, property acquired by the estate or by the debtor after the commencement of the case is not subject to any lien resulting from any security agreement entered into by the debtor before the commencement of the case.
>
> (b) Except as provided in sections 363, 506(c), 522, 544, 545, 547, and 548 of this title, if the debtor and an entity entered into a security agreement before the commencement of the case and if the security interest created by such security agreement extends to property of the debtor acquired before the commencement of the case and to proceeds, products, offspring, rents, or profits of such property, then such security interest extends to such

> proceeds, products, offspring, rents, or profits acquired by the estate after the commencement of the case to the extent provided by such security agreement and by applicable non-bankruptcy law, except to any extent that the court, after notice and a hearing and based on the equities of the case, orders otherwise.

In ruling that the monies generated post-petition under the Armco contract were subject to the Banks' lien, the Fourth Circuit relied exclusively upon the decision in In re Sunberg, 729 F.2d 561 (8th Cir. 1984). In Sunberg, the debtors had signed applications and contracts to participate in a federal payment-in-kind ("PIK") program prior to filing their petition in bankruptcy. Briefly, under the program, a farmer receives crops for not planting certain acreage. To secure their indebtedness to Production Credit Association ("PCA"), the debtors granted a security interest in certain collateral

including contract rights, accounts and general intangibles to PCA. The court ruled that the PIK contract was a general intangible which was in existence before the bankruptcy petition was filed, and therefore, the PIK benefits received by the debtor post-petition were subject to PCA's security interest. See also, In re J. Catton Farms, Inc., 779 F.2d 1242 (7th Cir. 1985).

The facts in Sunberg are clearly distinguishable from the facts in this case. In Sunberg, the debtors' right to receive PIK benefits was automatic. The debtors merely had to agree to leave certain acreage fallow. The debtors' right to receive PIK benefits was clearly established as of the filing of the bankruptcy petition.

However, in Slab Fork's case, its right to receive monies under the

Armco contract as of the filing of the bankruptcy petition was uncertain. As of the filing of the petition, all coal deliveries had been suspended; Armco had declared the situation to be one of excusable default under the contract. The only monies to which Slab Fork was entitled to under the Armco contract as of the filing of the petition were paid to the Banks. These monies were for coal sold and delivered pre-petition.

The Fourth Circuit's decision is contrary to the line of cases which hold that in order for a pre-petition security interest to extend to property received by a debtor post-petition, the debtor must have an absolute right to receive such property prior to the filing of the petition. In re Gross-Feibel Co., Inc., 21 B.R. 648 (Bankr. S.D. Ohio 1982); In re Northeast Chick Services, Inc., 43 B.R.

326 (Bankr. Mass. 1984); In re All-Brite Sign Service Co., Inc., 11 B.R. 403 (Bankr. W.D. Ky. 1981). As of the filing of the petition, Slab Fork had no entitlement to any additional monies from Armco; Slab Fork's right to receive monies post-petition was conditioned upon its ability to mine and deliver coal to Armco.

The Fourth Circuit's decision is also contrary to the ruling in In re Lawrence, 41 B.R. 36 (Bankr. Minn. 1984). In Lawrence, the debtor granted a pre-petition security interest to the bank in all existing and after-acquired farm products and their proceeds. The court held that the bank's lien did not extend to milk or milk proceeds produced by the debtor's cows post-petition. The court ruled that "milk produced post-petition is an asset coming into existence totally after the filing and not intended to be

covered by the 552(b) exception." Lawrence at 38. Similarly, the coal mined and delivered post-petition was an asset produced after the filing of Slab Fork's petition and should not be subject to the Banks' lien.

The monies generated post-petition under the Armco contract constitute after-acquired property and not proceeds. Proceeds are defined as "whatever is received upon the sale, exchange, collection or other disposition of collateral or proceeds." W. Va. Code, § 46-9-306 (1985 Cum. Supp.). The monies generated post-petition under the Armco contract were the result of the performance of the contract, not a product or proceed of the contract. Thus, under 11 U.S.C. § 552(a) the Banks' lien should not attach to the post-petition revenues under the Armco contract. The Fourth Circuit's ruling

that the monies generated under the Armco contract post-petition are proceeds of the Armco contract should be reversed.

B. The Rehabilitative Purpose of the Bankruptcy Code Issue.

In enacting the Bankruptcy Reform Act of 1978, and specifically Chapter 11 thereof, Congress provided an opportunity for insolvent entities to reorganize. The Fourth Circuit's decision in this case severely restricts a debtor's reorganization efforts. This case affords the Court the opportunity to address the issue of the competing needs of financial institutions and persons in bankruptcy and the protection afforded to them under the Bankruptcy Code. This case presents an issue of national importance which affects all businesses and lending institutions.

The purpose of Chapter 11 is rehabilitative in nature; the debtor is

afforded a "fresh start" and the opportunity to reorganize. In order to facilitate the debtor's reorganization efforts, the debtor is relieved of some of the onerous burdens of his prior transactions. In particular, the Bankruptcy Code provides that pre-petition security interests do not extend to property acquired by the debtor post-petition. The reason for such curtailment is based upon the realization that if pre-petition security interests were permitted to extend to after-acquired property the debtor's post-petition efforts would be frustrated since such efforts would be for the sole benefit of the secured creditor. The Fourth Circuit's decision in this case is in direct contravention of the purposes of the Bankruptcy Code.

The general rule of 11 U.S.C. § 552(a) which provides that a creditor's

pre-petition security interest does not extend to property acquired by the estate after the filing of the petition is an explicit embodiment of the fresh start policy underlying the entire Bankruptcy Code. The exception to the general rule set forth in 11 U.S.C. § 552(b) "was intended to protect a creditor's interest in particular pre-petition goods or collateral from being terminated by the filing of a bankruptcy petition." Lawrence, at 37 (citing 124 Cong. Rec. H. 11,097-11,098 (Sept. 28, 1978); S. 17,414 (Oct. 6, 1978)). Section 552(b) was intended to protect a creditor's security interest in collateral existing pre-petition from being cut off midstream by a bankruptcy. Lawrence, at 37-38.

The Banks were paid almost $1 million, which monies were collected post-petition but represented monies

earned for coal sold to Armco prior to the filing of the petition. Those monies are all the Banks are entitled to under 11 U.S.C. § 552(b). Moreover, since no deduction was made from the payment to the Banks for any costs incurred with respect to the mining of the coal sold pre-petition, those monies are all the Banks could reasonably expect to receive as a result of their security interest in the Armco contract. Upon payment of all monies due and owing under the Armco contract as of the date of the filing of the petition, the Banks received the benefit of their security interest in the Armco contract.

The Fourth Circuit has misconstrued the breadth of coverage of the exception under 11 U.S.C. § 552(b). A security interest created by a pre-petition security agreement only extends

to "proceeds, product, offspring, rents or profits" of "property of the debtor acquired before the commencement of the case". Section 552 contemplates that the affairs of the debtor are to be frozen as of the date of the filing of the petition. The secured creditor's security interest extends to proceeds of property in existence as of that date. Despite an after-acquired clause to the contrary, a pre-petition security interest does not extend to a debtor's after-acquired property. See In re Northeast Chick Services, Inc. As the court stated in In re Texas Tri-Collar, Inc., 29 B.R. 724, 727 (Bankr. W.D. La. 1983),

> An order allowing a prepetition security interest to extend to property acquired by the debtor after commencement of the case would be in contravention of section 552(a) and its goal of bolstering the debtor's fresh start.

If the Fourth Circuit's decision is per-

mitted to stand, Slab Fork's rehabilitation efforts, as well as numerous other similarly situated debtors, will have been frustrated. Slab Fork's efforts of engaging a contract miner to fulfill its obligations to Armco will have been for the exclusive benefit of the Banks.

Today's financing arrangements typically involve secured transactions. Most prudent lenders obtain a security interest in all of the borrower's properties existing as of the date of the loan and all property acquired by the borrower after the date of the loan. The Fourth Circuit's decision will thus have a profound effect on a Chapter 11 debtor's ability to reorganize. If a pre-petition security interest in a contract right is found to extend to all post-petition monies generated thereunder, then in the vast majority of Chapter 11 cases a

debtor's reorganization efforts will be for the sole benefit of the secured creditor. Such a result nullifies the very purpose of Chapter 11 reorganizations. Chapter 11 affords the debtor the opportunity to reorganize in order that its general unsecured creditors can be paid at least a percentage of their claim. The Fourth Circuit's decision, which is in contravention of the very purpose of the Bankruptcy Code, must be reversed.

C. The Cash Collateral Issue.

The Fourth Circuit determined that the monies generated post-petition under the Armco contract were cash collateral. In so ruling the Fourth Circuit relied upon the definition of cash collateral as modified by the Bankruptcy Amendment and Federal Judgeship Act of 1984. The 1984 Act was enacted in July, 1984,

one year after this issue was presented below to the Bankruptcy Court. The definition of cash collateral under the 1984 Act differs materially from the definition of cash collateral under the Bankruptcy Reform Act of 1978.

Section 363(a) of the Bankruptcy Reform Act of 1978 defined "cash collateral" as "cash, negotiable instruments, documents of title, securities, deposit accounts, or other cash equivalents in which the estate and an entity other than the estate have an interest". A study of the legislative history of this section reveals that the House Amendment contained in H.R. No. 8200, (124 Cong. Rec. H. 11,093 (Sept. 28, 1978)), had originally defined "cash collateral" as "inventory, accounts, contract rights, general intangibles, cash, negotiable instruments, documents of title, securities, or chattel

paper in which the estate and an entity other than the estate have an interest". However, the Senate version of the definition of "cash collateral", which is the version which was adopted and enacted, deleted inventory, accounts, contract rights, general intangibles, and chattel paper from the definition, "to remove limitations that were placed on the use, lease, or sale of such properties by the trustee or debtor-in-possession." 124 Cong. Rec. S. 17,409 (Oct. 6, 1978). Therefore, it is clear that at the time of the filing of Slab Fork's bankruptcy petition contract rights and accounts were specifically excluded from the definition of cash collateral.

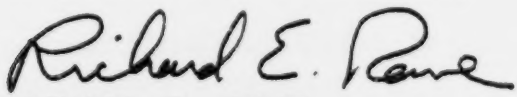
The definition of cash collateral under the 1984 Act extended the definition to include "proceeds, products, offspring, rents or profits of property

subject to a security interest as provided in section 552(b) of this title." 11 U.S.C. § 363(a). The Fourth Circuit's reliance on this language which was not a part of the definition at the time this issue was presented to the Bankruptcy Court is in error. Thus, the Fourth Circuit's ruling that the revenues generated post-petition under the Armco contract constitute cash collateral must be reversed.

CONCLUSION

For the foregoing reasons, the petition for a writ of certiorari should be granted.

Respectfully submitted,



RICHARD E. ROWE
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Attorneys for Petitioner,
Slab Fork Coal Company

Dated: May 2, 1986

CERTIFICATE

I hereby certify that Appellant Printing Services as agent for me has this 1st day of May, 1986, mailed the required copies of this Petition for a Writ of Certiorari and Appendix to Benjamin C. Ackerly and Gordon F. Rainey, Jr., at Hunton & Williams, 707 East Main Street, Post Office Box 1535, Richmond, Virginia, 23212; Marshall C. Spradling and Frederick L. Thomas, Jr., at Spilman, Thomas, Battle & Klostermeyer, Post Office Box 273, Charleston, West Virginia, 25301; and Jeffrey L. Tarkenton, Hunton & Williams, 2000 Pennsylvania Avenue, N.W., Post Office Box 19230, Washington, D.C., 20036, attorneys for Appellants, United Virginia Bank, Kanawha Valley Bank, N.A., and The Charleston National Bank.

Richard E. Rowe

RICHARD E. ROWE

APPENDIX

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APPENDIX A

UNITED STATES COURT OF APPEALS
FOR THE FOURTH CIRCUIT

No. 85-1228

United Virginia Bank;
Kanawha Valley Bank, N.A.;
The Charleston National Bank,

Appellants,

v.

Slab Fork Coal Company,

Appellee.

In Re: Slab Fork Coal Company

Debtor.

Appeal from the United States District Court for the Southern District of West Virginia, at Beckley. Charles H. Haden, II, District Judge. (CA 83-5249)

Argued: November 7, 1985
Decided: March 3, 1986

Benjamin C. Ackerly (Gordon F. Rainey, Jr; Vicki O. Tucker; Jeffrey L. Tarkenton; Hunton & Williams; Frederick L. Thomas, Jr.; Marshall C. Spradling; Spilman, Thomas, Battle & Klostermeyer on brief) for Appellants; Richard E. Rowe (Ellen A. Maxwell-Hoffman; Goodwin & Woodwin on brief) for Appellee.

P U B L I S H E D
784 F.2d 1188

MICHAEL: District Judge

This case is before the court on an appeal from the decision of the district court which upheld a bankruptcy court ruling. The issue presented is whether cash proceeds generated under a pre-bankruptcy petition contract for the supply of coal, which proceeds are received after the bankruptcy petition is filed, are subject to a pre-petition security interest in the contract and its proceeds.

The case comes before us on stipulated facts. Briefly stated, the appellee (hereinafter "Slab Fork") was brought into bankruptcy court by United Virginia Bank, and several other secured creditors (hereinafter "UVB") on an involuntary petition filed on 14 March 1983 under Chapter 7 of the Bankruptcy Code. Shortly thereafter,

the case was converted to a Chapter 11 bankruptcy proceeding.

For a number of years before the filing of the involuntary petition, Slab Fork had been party to a contract with Armco, Inc., under which Slab Fork sold coal that it had mined to Armco. This apparently was a profitable contract, and at the time the bankruptcy petition was filed, Armco was indebted to Slab Fork in an amount in excess of $900,000. This amount was paid by Armco and was considered by the Bankruptcy Court to be subject to UVB's pre-petition security lien. UVB thus received the benefit of that payment.

Apparently because the supply contract was profitable, Slab Fork, having shut down its own coal mining operation, made an agreement with Maben Coal Company (hereinafter "Maben") to mine and supply

coal to Armco for the account of Slab Fork. Under this arrangement, the original contract with Armco remained in effect. Armco apparently continued to pay Slab Fork, which in turn paid Maben for supplying coal to Armco. Slab Fork took the position that the cash thus generated post-petition was not covered by UVB's security interest. UVB then filed in the bankruptcy court a motion to prohibit the use of "excess" cash collateral, that is, the net cash receipts of Slab Fork from the post-petition coal shipments after the payment of appropriate expenses, including payment to Maben. Based upon a rather generalized application of § 363 of the Bankruptcy Code, the bankruptcy court held that the post-petition payments did not constitute cash collateral under § 363.

On appeal from the bankruptcy court's decision, the district court affirmed,

holding that although the post-petition receipts fell within the provisions of § 552 of the Bankruptcy Code, the post-petition proceeds were property acquired post-petition and thus were not subject to any security lien arising from the pre-petition agreement. However, in what apparently was the basic underpinning of the opinion below, the District Court further held that depriving Slab Fork of these receipts would seriously undermine the rehabilitative purposes of the Bankruptcy Code.

The District Court correctly held below that the matter was regulated by § 552(b) of the Bankruptcy Code. That section provides that:

> . . . if the debtor and an entity entered into a security agreement before the commencement of the case and if the security interest created by such security agreement extends to property of the debtor acquired before the commencement

> of the case and to proceeds. . . of such property, then such security interest extends to such proceeds. . . acquired by the estate after the commencement of the case to the extent provided by such security agreement and by applicable nonbankruptcy law. . .

11 U.S.C. § 552(b) (1984). This provision, by its very terms, governs the present case. In addition, there exist no non-bankruptcy laws which would supercede § 552(b), or which would render it inapplicable to the present case.

We disagree with the District Court's ruling that the post-petition cash receipts were not subject to UVB's pre-petition security interest, for several reasons. First, it is undisputed that the shipping of coal by Maben to Armco post-petition was done pursuant to and in performance of the original supply contract between Armco and Slab Fork. It is similarly undisputed that the payment for the

coal received by Armco post-petition was the payment called for under the same contract between Slab Fork and Armco. It is likewise undisputed that the pre-petition lien of UVB clearly covered the contract and such proceeds as might be derived from that contract.

These facts are nearly identical to the facts in In Re Sunberg, 729 F.2d 561 (8th Cir. 1984), in which the Eighth Circuit Court of Appeals held that the post-petition proceeds of a contract were subject to a pre-petition security interest. In Sunberg, several farmers had entered into a payment-in-kind agreement with the United States Department of Agriculture, under which the farmers received cash or crops in return for agreeing to maintain their farm land, but to leave it fallow. Payments made under the payment-in-kind program were used to secure a pre-petition

loan from the Production Credit Association. The Production Credit Association had obtained a security interest in those payments before the filing of petitions in bankruptcy against the farmers. Based upon these facts, it was argued that the payments made under the payment-in-kind program after the commencement of the bankruptcy cases were in fact property acquired after the commencement of those bankruptcies, and therefore were not subject to the Production Credit Association's lien. In its opinion, the Eighth Circuit stated:

> The Sunbergs attempt to avoid the lien on their PIK [payment-in-kind] benefits by characterizing those benefits as property acquired after the commencement of their bankruptcy case under 11 U.S.C. § 552(a) (1982). If PCA's [Production Credit Association's] security interest covered the PIK contracts and the proceeds of pledged collateral prior to the Sunbergs' petition in bankruptcy, however, the proceeds of

> those contracts realized after the petition would continue to be encumbered absent a bankruptcy court order to the contrary based on the equities of the particular case. Id. § 552(b).

729 F.2d at 562. The court in Sunberg thus determined, as Slab Fork correctly notes in its brief, that the rights to the payments-in-kind represented general intangibles in existence before the bankruptcy petitions were filed and were thus subject to the creditor's pre-petition security interest.

Applying this reasoning to the present case, the rights under Slab Fork's contract with Armco were likewise intangible rights, and were subject to UVB's lien before the filing of the bankruptcy petition. It is true that coal had to be supplied to Armco by or for Slab Fork before any right to payment arose, but that is true for all the payments under

the contract, whether generated pre-petition or post-petition. No change in the right to payment under the Armco contract was brought about by the filing of a bankruptcy petition, where the underlying asset and all proceeds therefrom were subject to a valid pre-petition security interest. This case thus falls squarely within the reasoning of Sunberg, and we adopt and apply the Eighth Circuit's holding in Sunberg to the present case.

On a second point, Slab Fork argues, and the court below held, that the proceeds in question were not "cash collateral" as that term is defined in § 363(a) of the Bankruptcy Code. That contention, however, does not find support in the Bankruptcy Amendment and Federal Judgeship Act of 1984. In the 1984 Act, Congress provided a statement of what constituted "cash collateral". That statement,

contained in an addition to § 363(a), says that cash collateral "includes the proceeds, products, offspring, rents or profits of property subject to a security interest as provided in § 552 of this title, whether existing before or after the commencement of a case under this title ..." Pub. L. 98-353, § 442(a)(1). This additional language clearly indicates Congress' intent as to the scope of "cash collateral" and to include in that definition circumstances such as those existing in the present case.

Notwithstanding our decision today, it should be noted that § 552(b) gives the bankruptcy court considerable latitude in applying pre-petition security interests to post-petition proceeds. As evidenced by the final clause in § 552(b), a bankruptcy court may choose not to apply a pre-petition security interest to post-

petition proceeds "based on the equities of the case." It appears clear from the legislative history related to § 552 that Congress undertook in that section to find an appropriate balance between the rights of secured creditors and the rehabilitative purposes of the Bankruptcy Act. The latitude afforded to the bankruptcy court seems to this court to indicate that such a balancing of interests was intended in the framing of § 552. In this case, the record does not reflect adequately the various equitable considerations which may bear on this question, and in any event such a determination should more properly be made in the first instance by the Bankruptcy Court.

For the reasons stated, the judgment of the court below is reversed, and the case is remanded to the district court for

further remand to the bankruptcy court, for such proceedings as may be appropriate in accordance with the provisions of § 552(b) and with this opinion.

REVERSED AND REMANDED.

APPENDIX B

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF WEST VIRGINIA
BECKLEY DIVISION

UNITED VIRGINIA BANK, et al.

Plaintiffs,

vs. CIVIL ACTION NO. 83-5249

SLAB FORK COAL COMPANY,

Defendant.

ORDER

Entered: February 2, 1985

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On May 30, 1984, this Court heard oral argument on the appeal of United Virginia Bank, Kanawha Valley Bank, N.A., and the Charleston National Bank (hereinafter Banks) from the order of the Bankruptcy Court for the Southern District of West Virginia denying the Banks' motion to prohibit the debtor's, Slab Fork Coal Company's, use of cash collateral. At the conclusion of the hearing the Court denied the Banks' appeal and affirmed the decision of the Bankruptcy Court. The Banks now move the Court to reconsider its ruling. The Court declines to do so for the following reasons:

1. The post-petition proceeds of the sale of coal by the Debtor to Armco, Inc. pursuant to a coal sales contract subject to a pre-petition security interest held by the Banks, is "property acquired by the estate or by the debtor

after the commencement of the case" under §552(a); further none of the exceptions set forth in §552(b) apply. Therefore, the cash generated by Debtor's sale of coal to Armco, Inc. is not subject to the Banks' pre-petition security interest.

2. The revenue generated through the post-petition sale of coal to Armco, Inc. is not "cash collateral" within the meaning of §363(a) and is not subject to the Banks' security interest in the contract.

3. Adopting the Banks' proposed position would seriously hamper a rehabilitating debtor's "fresh start" by encumbering revenue earned by post-petition operations. The Banks' argument tacitly recognizes this, in that the Banks concede they are not entitled to all of the proceeds from the post-petition coal sales to

Armco, Inc. but only that portion exceeding the Debtor's operating costs.

For the reasons enumerated above, the Court hereby denies the Banks' motion to reconsider and affirms the ruling of the Bankruptcy Court denying the Banks' motion to prohibit the Debtor's use of cash collateral.

The Clerk is directed to send a certified copy of this Order to counsel of record and to remove this action from the docket of this Court.

ENTER: 2/2/85

/s/ CHARLES H. HADEN, II
Charles H. Haden II, Chief Judge

APPENDIX C

IN THE UNITED STATES BANKRUPTCY COURT
FOR THE SOUTHERN DISTRICT OF WEST VIRGINIA

In re

SLAB FORK COAL COMPANY,

Debtor.

Case No. 83-50050
Chapter 11
Reorganization

ORDER DENYING MOTION OF BANKS TO
PROHIBIT USE OF CASH COLLATERAL

Entered: July 11, 1983

This 30th day of June, 1983, came the United Virginia Bank, Kanawha Valley Bank, N.S., and The Charleston National Bank (collectively the "Banks") by their attorneys Benjamin F. Ackerly, Vicki O. Tucker and Marshall C. Spradling, and also came the debtor Slab Fork Coal Company by its attorneys Richard E. Rowe and Thomas R. Goodwin, and this matter came on to be heard on the Banks' Motion to Prohibit Use of Cash Collateral in the form of receivables arising under the Slab Fork contract with Armco, from the sale of coal to Armco after the conversion to Chapter 11; and the Court heard the statements and arguments of Counsel, the respective exhibits which were entered into evidence, and the brief of the parties and after considering all of such, the Court is of the opinion for the reasons more fully stated on the record that neither the money received to

date nor future expectation of funds is cash collateral within the purview of Title 11 §363 and that accordingly it is hereby Ordered that the Banks' motion to prohibit the use of funds or to provide adequate protection for their use is denied, to all of which the Banks object and except.

ENTER: July 11, 1983

/s/ EDWIN L. FLOWERS
Judge Edwin F. Flowers, U.S. Bankruptcy Court for the Southern District of West Virginia

Approved for entry:

/s/ F. L. THOMAS, JR.
Counsel for the Banks
Seen and objected to

/s/ SUSAN C. WITTEMEIER
Counsel for Slab Fork Coal Company